

Message Text

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ACTION ARA-14

INFO OCT-01 ISO-00 SP-02 ICA-11 AID-05 EB-08 NSC-05
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FM AMEMBASSY LA PAZ
TO SECSTATE WASHDC PRIORITY 2009
INFO AMEMBASSY BOGOTA

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FOR: TREASURY TURBAY INAUGURATION DELEGATION

EO 11652: NA
TAGS: EGEN, EFIN, BL
SUBJECT: ECONOMIC BRIEFING MATERIAL FOR SECRETARY BLUMENTHAL

1. THIS TELEGRAM TRANSMITS A SUMMARY OF THE BOLIVIAN BALANCE OF PAYMENTS AND GENERAL ECONOMIC SITUATION AT MID-YEAR AS BACKGROUND INFORMATION FOR ANY POSSIBLE DISCUSSIONS WITH BOLIVIAN PRESIDENT JUAN PEREDA DURING THE COLOMBIAN PRESIDENTIAL INAUGURATION IN BOGOTA ON AUGUST 7.

2. BOLIVIA'S EXTERNAL SECTOR SO FAR IN 1978 HAS BEEN CHARACTERIZED BY: 1) MODERATELY STRONG DEMAND FOR IMPORTS; 2) DECLINING EXPORTS DUE TO DECREASED TIN AND PETROLEUM PRODUCTION; 3) TRADITIONAL HIGH SERVICES ACCOUNT BECAUSE OF BOLIVIA'S LANDLOCKED STATUS AND INCREASED THIS YEAR BECAUSE OF PRODUCTION SHARING PAYMENTS TO NEWLY PRODUCING US OIL COMPANIES; 4) CONTINUED MODERATELY HEAVY SHORT-TERM CAPITAL FLIGHT DUE TO POLITICAL UNCERTAINTY; 5) A SURPLUS ON THE LONG-TERM CAPITAL ACCOUNT BASED ON FOREIGN BORROWING BUT INCREASINGLY OFFSET BY INTEREST AND AMORTIZATION PAYMENTS; 6) AN ALARMING INCREASE OF COMMERCIAL BANK FOREIGN LIABILITIES.

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THE BOLIVIAN ECONOMIC SITUATION IS DIFFICULT BUT NOT YET DESPERATE, HOWEVER, ECONOMIC POLICY OPTIONS FOR THE GOB HAVE BEEN LIMITED BY THE PRE-ELECTORAL PROCESS PRIOR TO JULY 9, AND NOW A WEAK PEREDA GOVERNMENT. THE STRONG POLITICAL BASE NECESSARY TO CARRYOUT AUSTERE ECONOMIC MEASURES HAS BEEN LACKING.

3. THE CURRENT ACCOUNT IS CHARACTERIZED BY IMPORTS GROWING AT A MODERATELY HIGH RATE OF 12 PERCENT IN THE FIRST THREE MONTHS AND INCREASING TO ABOUT 16 PERCENT IN APRIL THROUGH JUNE, WHILE EXPORTS ARE LESS THAN PROJECTED DUE TO LOWER PETROLEUM AND TIN PRODUCTION AND TUNGSTEN PRICES. THE EXPORT PICTURE HAS BEEN SAVED FROM BEING MORE BLEAK BY VERY HIGH TIN PRICES. THERE IS NO CHANCE OF DRAMATIC IMPROVEMENT IN EXPORT PERFORMANCE IN THE SHORT RUN ALTHOUGH NATURAL GAS AND OIL EXPORTS WILL IMPROVE IN 1979. THE SHORT-TERM CAPITAL ACCOUNT HAS EXPERIENCED A LOW \$14 MILLION OUTFLOW IN THE FIRST QUARTER BUT WHAT THE YEAR END SHORT-TERM CAPITAL POSITION WILL BE DEPENDS IN LARGE PART ON THE UNFOLDING OF POLITICAL EVENTS IN THE SECOND HALF OF 1978. THE LONG-TERM CAPITAL ACCOUNT IS LESS THAN PREVIOUSLY PROJECTED ESSENTIALLY BECAUSE THE GOB IS RESTRICTING BORROWING BY COMIBOL AND YPFB (STATE MINING AND PETROLEUM COMPANIES). TWENTY MILLION DOLLARS OF IMF TRUST FUND FINANCING HAS BEEN ADDED TO THE EMBASSY ESTIMATE. THE LEVEL OF CENTRAL BANK OFFICIAL INTERNATIONAL RESERVES AS OF THE END OF JULY IS \$201 MILLION, INCLUDING RECEIPTS FROM THE IMF TRUST FUND. HOWEVER, THE POTENTIAL OUTSTANDING CLAIMS ON OFFICIAL RESERVES AS OF JULY 30 ARE ESTIMATED TO BE ABOUT \$150 MILLION. THE CENTRAL BANK BELIEVES THAT THE BALANCE OF PAYMENTS NET DEFICIT FOR 1978 (OFFICIAL RESERVES) WILL BE \$75 MILLION BUT THE EMBASSY ESTIMATE IS \$93 TO \$213 MILLION WITH THE MOST LIKELY OUTCOME BEING TOWARD THE LOWER END OF THAT SCALE. OF SPECIAL CONCERN IS THE LARGE DROP IN NET RESERVES OF THE CONSOLIDATED BANKING SYSTEM WHICH LIMITED OFFICIAL USE

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DROPPED 25 PERCENT TO \$110 MILLION FROM DECEMBER 1977 TO MAY 1978. FOREIGN BORROWINGS BY LOCAL BANKS HAVE CAUSED COMMERCIAL BANK INTERNATIONAL RESERVES TO DETERIORATE FROM MINUS \$57.6 MILLION AT THE END OF

1977 TO MINUS \$93 MILLION ON JUNE 30, 1978. THIS LARGE POTENTIAL CLAIM ON THE SYSTEM'S RESERVES COULD MEAN THAT RESERVES OF THE CONSOLIDATED SYSTEM WILL BE CLOSE TO ZERO BY YEAR END. BOLIVIA'S EXTERNAL DEBT AT MID-1978 IS ABOUT \$2.6 BILLION (SIGNED) WITH DISBURSEMENTS ABOUT \$1.8 BILLION. THE DEBT SERVICE RATIO FOR 1978 IS EXPECTED TO REACH 25 PERCENT. DURING THE FIRST SIX MONTHS OF 1978 TOTAL LIQUIDITY INCREASED BY ONLY 4.3 PERCENT AS A RESULT OF DECLINING INTERNATIONAL RESERVES (\$45 MILLION) AND A POLICY OF THE CENTRAL BANK TO LIMIT LIQUIDITY.

4. IT APPEARS THE NEW GOVERNMENT COULD GET THROUGH 1978 WITHOUT TAKING TOUGH AUSTERITY MEASURES BUT AT LEAST SOME MEASURES BEYOND THOSE ALREADY TAKEN MUST BE DECIDED UPON IN ORDER TO COMPLY WITH PROMISES MADE TO THE IMF AND TO END THE YEAR WITH AN ACCEPTABLE LEVEL OF RESERVES. IN OUR VIEW IT WOULD BE A MISTAKE FOR THE NEW GOVERNMENT TO AVOID TAKING AUSTERITY MEASURES SUCH

AS INCREASING RESERVE REQUIREMENTS, TIGHTENING CREDIT, INCREASING GASOLINE AND KEROSENE PRICES, INCREASING INTEREST RATES, IMPOSING PRIVATE AND PUBLIC DEBT CEILING, REDUCING OR LIMITING COMMERCIAL BANK FOREIGN SHORT-TERM LIABILITIES AND FURTHER CUTTING DEFICITS OF STATE ENTITIES. MEASURES ALREADY TAKEN WHICH HAVE BEEN PARTLY SUCCESSFUL IN BOLSTERING THE BALANCE OF PAYMENTS AND SLOWING THE RATE OF INCREASE IN DOMESTIC INFLATION INCLUDE A 20 PERCENT CUT IN THE BUDGETS OF THE STATE CORPORATIONS, RESTRICTIONS IN BANK CREDIT AND INCREASES IN SOME MINOR TAXES. AT THIS POINT NEITHER THE GOB NOR THE IMF (NOR THE EMBASSY) BELIEVE THAT A DEVALUATION IS REQUIRED DURING THE NEXT SIX TO NINE MONTHS. THE NEW GOVERNMENT COULD AVOID TAKING NECESSARY AUSTERITY MEASURES BY INCURRING MORE DEBT FROM COMMERCIAL SOURCES COMBINED WITH DRAWING DOWN RESERVES TO MEET FOREIGN EXCHANGE LIMITED OFFICIAL USE

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OBLIGATIONS. HOWEVER, SEEKING IMF ASSISTANCE AND TAKING AUSTERITY MEASURES IS THE PREFERRED COURSE BECAUSE THE OPPOSITE WILL ONLY POSTPONE THE INEVITABLE.

NOTE BY OC/T: SECTION 2 OF 2, LA PAZ 6257 NOT YET RECEIVED IN DEPARTMENT. WILL FOLLOW.

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ACTION ARA-14

INFO OCT-01 ISO-00 SP-02 ICA-11 AID-05 EB-08 NSC-05
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TO SECSTATE WASHDC PRIORITY 2010
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FOR: TREASURY TURBAY INAUGURATION DELEGATION

5. THE NEW GOVERNMENT WILL HAVE TO DEAL WITH SOME TOUGH ECONOMIC PROBLEMS AND THEIR POLITICAL IMPLICATIONS SOON. THE NEW GOB IS FACED WITH PUTTING TOGETHER A NEW ECONOMIC PACKAGE TO DEAL WITH SHORT-TERM PROBLEMS AND FORMULATE A STRATEGY TO DEAL WITH LONGER-TERM ECONOMIC PROBLEMS. SOME DIFFICULTS ECONOMIC DECISIONS WILL HAVE TO BE TAKEN, SHORT OFF DEVALUATION, TO DEAL WITH THE INHERITED ECONOMIC PROBLEMS AS OUTLINE ABOVE. THE IMF HAS PROVIDED (JUNE 30) ABOUT \$49 MILLION IN COMPENSATORY, TRUST FUND AND GOLD TRANCHE FINANCING. GOLD TRANCHE AND COMPENSATORY FINANCING WILL INCREASE LIQUIDITY BUT NOT RESERVES. A REGULAR IMF MISSION WILL VISIT BOLIVIA FOR AN ANNUAL COUNTRY REVIEW PROBABLY IN MID-OCTOBER. IF IT APPEARS THAT STANDBY FINANCING IS NEEDED THE NEW GOB CAN DISCUSS IT AT THAT TIME.

. BOLIVIA'S BALANCE OF PAYMENT
(US\$ MILLION)

	1977	1978	1978	1978
FINAL	REVISED	EMBASSY	EMBASSY	WORST
GOB	ESTIMATE	CASE	ESTIMATE	

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	TARGET			
CURRENT ACCT.				
1. EXPORTS (FOB)	649	657	627	609
2. IMPORTS (FOB)	(644)	(708)	(727)	(747)
3. SERVICES	(188.4)	(259)	(253)	(255)
4. TRANSFERS	15	20	20	20
5. BALANCE	(168.4)	(290)	(333)	(375)

CAPITAL ACCT				
1. LONG TERM				
CAPITAL NET	338	298	330	335
2. SHORT TERM				
CAPITAL NET	(123)	(83)	(90)	(175)
3. BALANCE	214	215	240	160
ERRORS & OMISSIONS	(38.9)	--	--	--
NET BALANCE	7.7	(75)	(93)	(213)

NOTE: THE BASIC DIFFERENCE IN THE EMBASSY WORST CASE ESTIMATE IS A LOWER VOLUME OF TIN PRODUCTION, LARGER SHORT-TERM CAPITAL OUTFLOW AND LARGER IMPORTS.

7. GENERAL ECONOMIC-THE AUSTERITY MEASURES BEING TAKEN BY THE GOB TO HOLD DOWN LIQUIDITY MAY NOT ONLY HAVE THE DESIRED IMPACT ON RESTRAINING IMPORTS AND REDUCING THE BUDGET DIFICIT BUT WILL HAVE A DAMPENING EFFECT ON THE GROWTH RATE OF THE BOLIVIAN ECONOMY. IT IS PROBABLE THAT THE GROWTH RATE WILL BE EVEN LESS THAN THE ALREADY MODEST PREDICTION OF 5 PERCENT. PERHAPS 2 TO 3 PERCENT. CREDIT RESTRICTION AND BUDGET DEFICIT REDUCTION ARE ANTI-INFLATIONARY MEASURES BUT ALSO RESTRICT ECONOMIC

ACTIVITY. OFFSETTING THIS
ANTI-INFLATINARY EFFECT SOMEWHAT WILL BE SLIGHT PRESSURE ON
PRICES OF DOMESTICALLY PRODUCED GOODS THAT WILL BE THE OBJECT
OF CONSUMER DOLLARS DIVERTED FROM IMPORTS. HOWEVER,
WE EXPECT THAT DOMESTIC INFLATION WILL BE HELD TO ABOUT 18
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PERCENT THIS YEAR. THE LOWER LEVEL OF GROWTH FOR THE ECONOMY WILL
ALSO HAVE ITS POLITICAL COST AS UNEMPLOYMENT LEVELS ARE LIKELY
TO BE HIGER THIS YEAR THAN IN PREVIOUS YEARS. 1978 WILL
CONTRAST WITH THE RATHER STRONG PERFORMANCE OF THE ECONOMY OVER
THE PAST FEW YEARS. ECONOMIC GROWTH FOR THE PAST FIVE YEARS
HAS AVERAGED ALMOST 6 PERCENT PER ANNUM. THE NEW GOVERNMENT WILL
BE FACED WITH A BALANCING OF POLITICAL AND ECONOMIC CONSIDERATIONS
REGARDING THE COMPOSITION AND IMPLEMENTATION OF ITS ECONOMIC
PROGRAM.
BOEKER

NOTE BY OC/T: MESSAGE DELAYED IN TRANSMISSION.

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